

**NATIONAL GALLERY OF ART**

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**FINANCIAL STATEMENTS**  
**for the year ended September 30, 2009**  
**AND**  
**REPORT THEREON**

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**Report of Independent Auditors**

To the Board of Trustees of  
The National Gallery of Art

In our opinion, the accompanying statements of financial position and the related statements of activities and cash flows, present fairly, in all material respects, the financial position of the National Gallery of Art (the Gallery) at September 30, 2009, and the changes in its net assets and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Gallery's management; our responsibility is to express an opinion on these financial statements based on our audit. The prior year summarized comparative information has been derived from the Gallery's 2008 financial statements which have been adjusted to reflect the adoption of the *Not For Profit Entities* standard as described in Note 1, and in our report dated November 13, 2008 we expressed an unqualified opinion on those financial statements. We conducted our audit of these statements in accordance with auditing standards generally accepted in the United States of America and Government Auditing Standards issued by the Comptroller General of the United States, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note 1, the Gallery adopted the *Fair Value Measurements and Disclosures* standard and as discussed in Note 1, in fiscal year 2009 the Gallery adopted the *Not for Profit Entities* standard.

In accordance with Government Auditing Standards, we have also issued a report dated November 16, 2009, on our consideration of the Gallery's internal control structure and its compliance with laws and regulations.

*PricewaterhouseCoopers LLP*

November 16, 2009

**NATIONAL GALLERY OF ART**  
**STATEMENTS OF FINANCIAL POSITION**  
**September 30, 2009 and 2008**  
*with summarized financial information as of September 30, 2008*

(in thousands)

ASSETS

	Private Funds	Federal Funds	Total 2009	Total (as adjusted) 2008
Cash and cash equivalents	\$ 16,783	\$ 32,503	\$ 49,286	\$ 38,537
Accounts receivable, net	1,376	-	1,376	2,487
Pledges receivable, net	17,118	-	17,118	21,740
Investments	584,010	-	584,010	609,642
Trusts held by others	11,207	-	11,207	11,440
Publications inventory, net	1,282	-	1,282	1,672
Deferred charges and other assets	4,565	-	4,565	1,253
Fixed assets, net	64,161	131,182	195,343	191,790
Art collections	-	-	-	-
Total assets	<u>\$ 700,502</u>	<u>\$ 163,685</u>	<u>\$ 864,187</u>	<u>\$ 878,561</u>

LIABILITIES AND NET ASSETS

Liabilities:				
Accounts payable and accrued expenses	\$ 11,083	\$ 29,547	\$ 40,630	\$ 42,420
Capital lease obligation	-	1,716	1,716	1,884
Contractual obligations	33,688	-	33,688	31,808
Asset retirement obligation	-	19,746	19,746	19,150
Total liabilities	<u>44,771</u>	<u>51,009</u>	<u>95,780</u>	<u>95,262</u>
Net Assets:				
Unrestricted				
Investments in fixed assets, net of accumulated depreciation and amortization	64,161	129,466	193,627	189,906
Future funded expenses recognized	-	(31,837)	(31,837)	(30,627)
Total undesignated	<u>64,161</u>	<u>97,629</u>	<u>161,790</u>	<u>159,279</u>
Designated for collections and art purchases	9,781	-	9,781	19,826
Designated for special exhibitions	10,218	-	10,218	8,474
Designated for capital projects	15,123	-	15,123	15,683
Designated for education and public programs	7,414	-	7,414	7,157
Designated for other operating purposes	50,431	-	50,431	46,584
Designated for publications, including systematic catalogues	16,893	-	16,893	20,482
Total designated	<u>109,860</u>	<u>-</u>	<u>109,860</u>	<u>118,206</u>
Total unrestricted	174,021	97,629	271,650	277,485
Temporarily restricted	116,362	15,047	131,409	133,086
Permanently restricted	365,348	-	365,348	372,728
Total net assets	<u>655,731</u>	<u>112,676</u>	<u>768,407</u>	<u>783,299</u>
Total liabilities and net assets	<u>\$ 700,502</u>	<u>\$ 163,685</u>	<u>\$ 864,187</u>	<u>\$ 878,561</u>

*The accompanying notes are an integral part of these financial statements*

**NATIONAL GALLERY OF ART  
STATEMENTS OF ACTIVITIES**  
**for the years ended September 30, 2009 and 2008**  
*with summarized financial information for the year ended September 30, 2008*  
(in thousands)

	Unrestricted			Temporarily Restricted	Permanently Restricted	Total	
	Private Funds	Federal Funds	Total			2009	2008
<b>OPERATING</b>							
Support and revenue:							
U.S. Government appropriation	\$ -	\$ 100,580	\$ 100,580	\$ 3,350	\$ -	\$ 103,930	\$ 101,072
Gifts and grants	2,598	-	2,598	6,732	-	9,330	10,012
Gallery shop sales, net	7,772	-	7,772	-	-	7,772	10,049
Investment return designated for operations	5,617	-	5,617	11,346	-	16,963	1,036
Royalties and other income	1,505	-	1,505	-	-	1,505	2,245
	17,492	100,580	118,072	21,428	-	139,500	124,414
Net assets released from restrictions to fund operating expenses	18,305	3,388	21,693	(21,693)	-	-	-
Total support and revenue	35,797	103,968	139,765	(265)	-	139,500	124,414
Operating expenses:							
Program services:							
Collections	5,530	37,066	42,596	-	-	42,596	42,799
Special exhibitions	5,071	16,847	21,918	-	-	21,918	22,238
Education, gallery shops and public programs	16,321	28,389	44,710	-	-	44,710	46,036
Editorial and photography	2,198	3,321	5,519	-	-	5,519	5,254
Total program services	29,120	85,623	114,743	-	-	114,743	116,327
Supporting services:							
General and administrative	6,311	25,373	31,684	-	-	31,684	30,524
Development	3,076	1,589	4,665	-	-	4,665	4,620
Total supporting services	9,387	26,962	36,349	-	-	36,349	35,144
Total expenses	38,507	112,585	151,092	-	-	151,092	151,471
Decrease in net assets from operating activities	(2,710)	(8,617)	(11,327)	(265)	-	(11,592)	(27,057)
<b>NON-OPERATING</b>							
U.S. Government appropriation	-	-	-	17,368	-	17,368	17,736
Non-operating gifts and grants	3,300	-	3,300	12,999	792	17,091	18,642
Provision for bad debts	(2)	-	(2)	-	-	(2)	(3,927)
Other Income	163	-	163	-	-	163	-
Changes in value of trusts held by others	(148)	-	(148)	(14)	86	(76)	(1,345)
Investment return in excess of amount designated for operations	1,338	-	1,338	(7,504)	-	(6,166)	(111,826)
Reclassifications of net asset balances	(2,076)	-	(2,076)	10,334	(8,258)	-	-
Net assets released from restrictions to fund non-operating expenses	20,602	13,993	34,595	(34,595)	-	-	-
Change in net assets from non-operating activities before acquisitions of works of art	23,177	13,993	37,170	(1,412)	(7,380)	28,378	(80,720)
Acquisitions of works of art	(31,678)	-	(31,678)	-	-	(31,678)	(12,793)
(Decrease) increase in net assets	(11,211)	5,376	(5,835)	(1,677)	(7,380)	(14,892)	(120,570)
Net assets at beginning of the year	190,094	92,253	282,347	128,224	372,728	783,299	903,869
Adoption of new accounting principle	(4,862)	-	(4,862)	4,862	-	-	-
Net assets at beginning of the year as adjusted	185,232	92,253	277,485	133,086	372,728	783,299	903,869
Net assets at end of the year	\$ 174,021	\$ 97,629	\$ 271,650	\$ 131,409	\$ 365,348	\$ 768,407	\$ 783,299

*The accompanying notes are an integral part of these financial statements*

**NATIONAL GALLERY OF ART**  
**STATEMENTS OF CASH FLOWS**  
**for the year ended September 30, 2009**  
*with summarized financial information as of September 30, 2008*  
(in thousands)

	Private Funds	Federal Funds	Totals	
			2009	2008
Cash flows from operating activities:				
(Decrease) increase in net assets	\$ (23,605 )	\$ 8,713	\$ (14,892 )	\$ (120,570 )
Adjustments to reconcile (decrease) increase in net assets to net cash (used in) provided by operating activities:				
Depreciation and amortization	3,685	5,978	9,663	9,819
Amortization of discount on pledges receivable	(544 )	-	(544 )	(761 )
Amortization of discount on contractual obligations	1,092	-	1,092	1,342
Provision for bad debts	2	-	2	3,927
Contributions and net investment income for permanently restricted investments	(3,767 )	-	(3,767 )	(14,260 )
U.S. Government appropriations for renovation projects	-	(17,368 )	(17,368 )	(17,736 )
Gifts and grants for art acquisitions and capital projects	(18,399 )	-	(18,399 )	(16,732 )
Acquisitions of works of art	32,238	-	32,238	20,257
Realized losses (gains) on sale of investments	22,712	-	22,712	(59,884 )
Unrealized (gains) losses on investments	(28,425 )	-	(28,425 )	179,208
Realized loss on sale of securities in trust held by others	-	-	-	700
Decrease in value of trusts held by others	232	-	232	2,029
Decrease (increase) in accounts receivable, net	1,108	-	1,108	(671 )
Decrease in pledges receivable, net	5,166	-	5,166	14,187
Decrease (increase) in publications inventory, net	390	-	390	(60 )
Increase in deferred charges and other assets	(3,311 )	-	(3,311 )	(48 )
(Decrease) increase in accounts payable and accrued expenses	(1,702 )	761	(941 )	1,343
Increase in contractual obligations	10,000	-	10,000	844
Increase in asset retirement obligation	-	882	882	914
Asset retirement remediation payment	-	(286 )	(286 )	(1,132 )
Net cash (used in) provided by operating activities	(3,128 )	(1,320 )	(4,448 )	2,716
Cash flows from investing activities:				
Purchase of investments	(82,469 )	-	(82,469 )	(411,936 )
Proceeds from sale of investments	113,815	-	113,815	407,063
Proceeds from sale of securities in trusts held by others	-	-	-	4,894
Acquisitions of works of art	(32,238 )	-	(32,238 )	(20,257 )
Purchase of fixed assets	(870 )	(13,194 )	(14,064 )	(17,035 )
Net cash used in investing activities	(1,762 )	(13,194 )	(14,956 )	(37,271 )
Cash flows from financing activities:				
Contributions and net investment income for permanently restricted investments	3,767	-	3,767	14,259
U.S. Government appropriation for renovation projects	-	17,368	17,368	17,736
Gifts and grants for art acquisitions and capital projects	18,399	-	18,399	16,732
Principal payment on capital lease obligation	-	(168 )	(168 )	(153 )
Payments on contractual obligations	(9,213 )	-	(9,213 )	(9,813 )
Net cash provided by financing activities	12,953	17,200	30,153	38,761
Net increase in cash and cash equivalents	8,063	2,686	10,749	4,206
Cash and cash equivalents, at beginning of year	8,720	29,817	38,537	34,331
Cash and cash equivalents, at end of year	\$ 16,783	\$ 32,503	\$ 49,286	\$ 38,537
Supplemental disclosure of cash flow information:				
Cash paid during the year for:				
Interest on capital lease	\$ -	\$ 172	\$ 172	\$ 186
Income taxes	\$ 30	\$ -	\$ 30	\$ 250
Supplemental disclosure of non-cash information:				
Donated investment securities	\$ 1,394	\$ -	\$ 1,394	\$ 4,621
Donated building	\$ 3,300	\$ -	\$ 3,300	\$ -
Fixed asset additions included in accounts payable	\$ -	\$ 1,247	\$ 1,247	\$ 2,095

*The accompanying notes are an integral part of these financial statements*

**NATIONAL GALLERY OF ART**  
**NOTES TO FINANCIAL STATEMENTS**  
(in thousands)

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**1. Summary of significant accounting policies**

**General**

The National Gallery of Art (the Gallery) receives an annual appropriation to cover its core programs as part of the budget approved annually by Congress and signed by the President. This is supplemented with income from endowments designated for current operating expenditures as well as gifts and grants designated by the donors for specific programmatic activity. (All monies, related activities and balances from federal sources are referred to herein as "federal", while all other monies, related activities and balances are referred to herein as "private".) All identified inter-fund transactions have been eliminated from the financial statements.

**Measure of operations**

The Gallery includes in its measure of operations all federal and private support and revenue and expenses that are integral to its core program services: collections; special exhibitions; education, gallery shops and public programs; and editorial and photography. The measure of operations excludes certain non-operating activities such as non-operating gifts and grants, investment return in excess of amounts designated for operations and acquisitions of works of art.

The Gallery's Board of Trustees designates only a portion of the Gallery's cumulative investment return for support of current operations; the remainder is retained to support operations of future years and offset potential market declines. The amount designated (a portion of which is computed under the spending policy) and all interest income earned by investing cash in excess of daily requirements are used to support current operations (see Note 5).

**Summarized financial information**

The financial statements include certain summarized prior-year information in total only, but not by net asset class. Such information does not include sufficient detail to constitute a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with the Gallery's financial statements for the year ended September 30, 2008 from which the summarized information was derived.

**NATIONAL GALLERY OF ART**  
**NOTES TO FINANCIAL STATEMENTS**  
**(in thousands)**

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**Net assets**

The Gallery's net assets, support and revenue, expenses, gains and losses are classified based on the existence or absence of donor-imposed restrictions. Accordingly, net assets of the Gallery are classified and reported as follows:

- *Unrestricted net* assets include "one-year" federal appropriations and all other resources, which are not subject to donor-imposed restrictions. One-year federal appropriations which are not obligated or expended are retained by the Gallery in accordance with federal guidelines. At the discretion of the Gallery's Board of Trustees, private funds which are not expended for operating activities may be set aside in designated reserves and earmarked to cover future program costs or other contingencies.
- *Temporarily restricted* net assets carry specific donor-imposed restrictions on the expenditure or other use of the contributed funds. In addition, the Gallery's "no-year" federal appropriations for special exhibitions, emergency response, and for the repair, renovation and restoration of its buildings are classified as temporarily restricted net assets.

Temporary restrictions may expire as a result of fulfillment of the donor's wishes or the passage of time. Net assets released from temporarily restricted net assets to unrestricted net assets occur when contributions are expended or time restrictions lapse and are reported as net assets released from restrictions in the statement of activities.

- *Permanently restricted* net assets have donor-imposed restrictions which stipulate that the corpus of the gifts be retained permanently. In some cases, the donor has also permanently restricted the use of excess income and any realized or unrealized gains attributable to the corpus.

**Cash and cash equivalents**

Cash and cash equivalents include interest-bearing demand deposits and appropriated amounts remaining on deposit with the U.S. Treasury. The Gallery considers all highly liquid investments with an original maturity of three months or less to be cash equivalents, except where such cash equivalents are held as part of a long-term investment strategy (see Notes 2 and 5).

**NATIONAL GALLERY OF ART**  
**NOTES TO FINANCIAL STATEMENTS**  
**(in thousands)**

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**Pledges receivable**

Unconditional promises to contribute to the Gallery in the future (pledges receivable) received are recorded at the fair value of future cash flows, using a risk-free rate of return, after providing an allowance for uncollectibility. Unconditional promises received prior to October 1, 2008, a risk-free rate of return at the date of the gift was used. For those unconditional promises received on or after October 1, 2008, a discount rate approximating the market rates for unsecured borrowing as required by a newly adopted accounting standard related to fair value determination is used (see Note 16). Conditional promises to give are recognized as income when the conditions stipulated by the donor are substantially met.

**Investments**

Investments are generally carried at fair value. Certain investments are valued using readily determinable market prices, while other investments are carried at the estimated fair value as provided by the investment managers. The Gallery reviews and evaluates the values provided by its investment managers and agrees with the valuation methods and assumptions they used in determining the fair value. The fair value of these other investments may be based on historical cost, appraisals, obtainable prices for similar assets, or other assets, or other estimates. Because of the uncertainty of valuation of these alternative investments, their values may differ from values that would have been used had a ready market for the investments existed.

Purchases and sales of securities are reflected on a trade-date basis. Gains and losses on sales of securities are based on average historical value (cost of securities if purchased or the fair market value at the date of gift if received by donation). Dividend and interest income is recorded on an accrual basis. In accordance with the policy of stating investments at fair value, the net change in unrealized appreciation or depreciation for the year is reflected in the statement of activities (see Notes 5 and 16).

**Trusts held by others**

The Gallery has been named as beneficiary in several irrevocable charitable trusts held by third parties. The Gallery's share of these trusts is recorded at current fair value. Income distributions from these trusts are recorded as investment income and changes in the value of these trusts are recorded as "changes in the value of trusts held by others" in the statement of activities.

**Publications inventory**

Publications inventory is carried at the lower of cost or market. Cost is determined using the average cost method.



**NATIONAL GALLERY OF ART**  
**NOTES TO FINANCIAL STATEMENTS**  
**(in thousands)**

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**Deferred charges and other assets**

Deferred charges represent private expenses incurred in connection with future special exhibitions and other activities and are recognized in the period in which the exhibition or activity occurs. Other assets largely represents private asset contributions to the Gallery which are recorded at fair value at the date of the gift.

**Fixed assets**

The land occupied by the Gallery's buildings was appropriated and reserved by the Congress of the United States for that purpose. No value has been assigned in the accompanying financial statements. Buildings are recorded at cost and depreciated on a straight-line basis over the estimated useful life of fifty years. Building improvements, equipment, furniture and computer software are also recorded at cost and depreciated on a straight-line basis over estimated useful lives ranging from five to twenty-five years. Upon retirement of fixed assets, the related cost and accumulated depreciation are removed from the accounts (see Note 8).

**Art collections**

The Gallery's art collections focus upon European and American paintings, sculpture and works on paper. In conformity with accounting policies generally followed by art museums, the value of art has been excluded from the statement of financial position. The Gallery's collections are maintained for public exhibition, education and research in furtherance of public service, rather than for financial gain.

The Gallery acquires its art collections through purchase or by donation-in-kind. Only current year purchases made from specifically designated funds, not donations-in-kind, are reflected in the statement of activities. The Gallery does not deaccession any of its permanent collections.

**Accrued leave**

Annual leave is accrued as it is earned by employees and is included in personnel compensation and benefit costs. An unfunded liability as of the date of the financial statements is recognized for earned but unused annual leave by federal employees since this annual leave will be paid from future federal appropriations when the leave is used by employees. The amount accrued is based upon current pay of the employees.

**NATIONAL GALLERY OF ART**  
**NOTES TO FINANCIAL STATEMENTS**  
**(in thousands)**

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**Employee benefits**

The Federal Accounting Standards Advisory Board issued Statement of Federal Financial Accounting Standards No. 5 (SFFAS No. 5), "Accounting for Liabilities of the Federal Government", which requires employing agencies to recognize the cost of pensions and other retirement benefits during their employees' active years of service. The pension expense recognized in the Gallery's financial statements is equal to the current service cost for the Gallery's employees for the accounting period less the amount contributed by the employees. The measurement of the pension service cost requires the use of an actuarial cost method and assumptions with factors applied by the Gallery. These factors are supplied by the Office of Personnel Management (OPM), the agency that administers the plan. The excess of the recognized pension expense over the amount contributed by the Gallery represents the amount being financed directly through the Civil Service Retirement and Disability Fund administered by OPM. This amount is considered imputed financing by the Gallery.

All permanent employees of the Gallery, both federal and non-federal, hired subsequent to January 1, 1984 participate in both the Social Security Retirement System and the Federal Employees' Retirement System (FERS). Employees hired prior to January 1, 1984 had the option of remaining under the Civil Service Retirement System (CSRS) or electing FERS. All employees have the option to make tax-deferred contributions to a Thrift Savings Plan and, in some instances, receive a matching portion from the Gallery. The Gallery funds all retirement contributions on a current basis, and accordingly there are no unfunded retirement costs (see Note 13).

SFFAS No. 5 also requires that the Gallery recognize a current-period expense for the future cost of post-retirement health benefits and life insurance for its employees while they are still working. The Gallery accounts for this expense in its financial statements in a manner similar to that used for pension expense, with the exception that employees and the Gallery do not make current contributions to fund these future benefits.

**Imputed financing sources**

In certain cases, the operating costs of the Gallery are paid out of funds appropriated to other Federal agencies. As an example, the law requires certain costs of retirement programs be paid by OPM and certain legal judgments against the Gallery be paid from the Judgment Fund maintained by Treasury. Costs that are identifiable to the Gallery and directly attributable to the Gallery's operations are paid by these Federal agencies.

**NATIONAL GALLERY OF ART**  
**NOTES TO FINANCIAL STATEMENTS**  
(in thousands)

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**Contributed services and donated assets**

The Gallery has volunteers who provide assistance in various departments. Such contributed services do not meet the criteria for recognition of contributed services contained in Accounting Standards Codification (“ASC”) Topic 958, “*Not-for-Profit Entities*”, and accordingly, are not reflected in the accompanying financial statements.

Donated assets, which do not become part of the Gallery’s art collections, are recorded at their fair value at the date of the gift. The Gallery does not imply time restrictions for gifts of long-lived assets. As a result, in the absence of donor-imposed restrictions, gifts of long-lived assets are reported as unrestricted revenue.

**Functional allocation of expenses**

The cost of providing various programs and other activities has been summarized on a functional basis in the statement of activities. Certain costs including depreciation, utilities, building maintenance, security and other operating costs have been allocated among program and supporting services.

Included under the Collections category are the costs of the care and display of the Gallery’s collections. Special exhibitions includes travel, transportation of items and other services necessary for the display of special exhibitions. Education, gallery shops and public programs includes the cost of providing a wide array of lectures, tours, films, music, symposia and academic programs to the general public, in addition to gallery shop cost of goods sold and expenses. Editorial and photography includes the costs to produce the many publications produced by the Gallery. General and administrative includes expenses for executive management, financial administration, information systems, human resources and legal services. Development includes the expenses associated with individual and corporate gifts and grants, annual appeals and other fundraising efforts.

**Estimates**

The preparation of the financial statements, in conformity with generally accepted accounting principles, requires management to make estimates and assumptions that affect the reported amount of assets and liabilities, disclosure of contingent assets and liabilities, and the reported amounts of support and revenue and expenses at the date of the financial statements and during the reporting period. Actual results could differ from these estimates.

**Reclassifications**

Certain prior year balances have been reclassified to conform to current year presentation.

**NATIONAL GALLERY OF ART**  
**NOTES TO FINANCIAL STATEMENTS**  
(in thousands)

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**Recently Issued Accounting Pronouncements**

Effective October 1, 2008, the Gallery adopted Accounting Standards Codification (“ASC”) Topic 820, “*Fair Value Measurements and Disclosures*” (“ASC Topic 820”), and ASC Topic 825-10-25 “*Financial Instruments - Recognition*” issued by the Financial Accounting Standards Board (FASB). See Note 16.

The Gallery adopted the ASC Topic 958-205-45, “*Endowments of Not-for-Profit Entities – Other Presentation Matters*”, at the beginning of the 2008 year. See Note 17.

On October 1, 2008, the Gallery adopted the provisions of ASC Topic 740-10-25, “*Income Taxes Recognition*” (“ASC Topic 740-10-25”). See Note 14.

**2. Cash and cash equivalents**

As of September 30, 2009 and 2008, cash and cash equivalents include federal cash of \$32,503 and \$29,817, respectively, on deposit with the U.S. Treasury representing appropriated amounts yet to be disbursed. There are no reconciling items between the amounts recorded by the Gallery and on deposit with the U.S. Treasury.

The Gallery places its cash in a financial institution that is federally insured for \$250 under the Federal Depository Insurance Corporation Act. At September 30, 2009 the aggregate balances were in excess of the insurance and therefore bear some risk since they are not collateralized.

**3. Accounts receivable, net**

As of September 30, 2009 and 2008, accounts receivable consisted of the following:

	2009	2008
Accrued investment income	\$ 556	\$ 532
Special exhibition and other program receivables	816	1,536
Other	53	453
Subtotal	1,425	2,521
Less: allowances	(49)	(34)
Total	\$ 1,376	\$ 2,487

**NATIONAL GALLERY OF ART**  
**NOTES TO FINANCIAL STATEMENTS**  
(in thousands)

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**4. Pledges receivable, net**

As of September 30, 2009 and 2008, pledges receivable consisted of the following:

	2009	2008
Due in one year or less	\$ 12,390	\$ 13,670
Due between one year and five years	7,375	11,046
Due in more than five years	302	369
Subtotal	20,067	25,085
Less: discounts of \$799 and \$1,180 and allowances of \$2,150 and \$2,165 respectively	(2,949)	(3,345)
Total	\$ 17,118	\$ 21,740

As of September 30, 2009, and September 30, 2008, \$1,724 and \$3,009 of the pledge receivable balance was receivable from related parties. The Gallery has received conditional promises to give of \$5,414 and \$6,086 as of September 30, 2009 and 2008, respectively.

**5. Investments**

As of September 30, 2009 and 2008, investments consisted of the following:

	2009		2008	
	Cost	Fair value	Cost	Fair value
Loan to the U.S. Treasury	\$ 5,000	\$ 5,000	\$ 5,000	\$ 5,000
Government obligations, cash and money market funds	-	-	7,442	7,442
Common and preferred stocks	63,949	69,255	77,346	71,070
Mutual funds	139,876	136,784	156,461	146,360
Alternative investments	352,348	372,971	369,094	379,770
Total	\$ 561,173	\$ 584,010	\$ 615,343	\$ 609,642

In 1942, the Gallery, under authority of an Act of Congress, made a \$5,000 permanent loan to the U.S. Treasury. This loan bears interest at 1/4% below the average monthly rate for long-term funds paid by the U.S. Treasury (ranging from 4.0% to 4.25% during fiscal year 2009). Interest income on this loan was \$206 and \$214 for the fiscal years ended September 30, 2009 and 2008, respectively.

**NATIONAL GALLERY OF ART**  
**NOTES TO FINANCIAL STATEMENTS**  
(in thousands)

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Investments in common and preferred stocks and mutual funds, limited partnerships and limited liability companies consist of the Gallery's ownership interest in externally managed investment funds, which invest in market-traded equity and fixed income securities.

The Gallery has capital commitments outstanding, related to various limited partnership interests it owns as of September 30, 2009 and 2008, totaling \$46,251 and \$52,495, respectively.

Alternative investments include investments in limited partnerships of \$192,997 and \$181,337, as of September 30, 2009 and 2008, respectively, that are considered to be "alternative investments" because they invest in marketable equity and fixed income securities. Alternative investments also include "other alternative investments" consisting of the Gallery's ownership interest in externally managed private equity, venture capital, multi-asset class, and hedge funds which are organized as limited partnerships. These investments may include certain types of financial instruments (among which are derivatives, futures and forward contracts, options, and securities sold not yet purchased) intended to hedge against changes in their market value. These financial instruments, which involve varying degrees of off-balance sheet risk, may result in losses due to changes in the market. Market values of investments may decline for a number of reasons, including changes in prevailing market and interest rates, increase in defaults and credit rating downgrades.

The following table summarizes the Gallery's holdings in alternative investments as of September 30, 2009 and 2008:

<u>Alternative Investment Type</u>	<u>2009</u>		<u>2008</u>	
	<u>Number of Funds</u>	<u>Fair value</u>	<u>Number of Funds</u>	<u>Fair value</u>
Public equity and income funds	6	\$ 192,997	5	\$ 181,337
Hedge funds	2	108,934	2	121,827
Multi asset class	1	40,468	1	43,487
Private Equity	11	22,026	11	25,305
Venture Capital	3	8,546	3	7,814
Total	<u>23</u>	<u>\$ 372,971</u>	<u>22</u>	<u>\$ 379,770</u>

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The following schedule summarizes the investment return and its classification in the statement of activities:

	<u>Unrestricted</u>	<u>Temporarily Restricted</u>	<u>Permanently Restricted</u>	<u>2009 Total</u>	<u>2008 Total</u>
Investment return designated for operations					
Interest on short-term investments	\$ 32	\$ -	\$ -	\$ 32	\$ 463
Investment return not designated by spending policy for operations	5,216	-	-	5,216	(14,902)
Investment return designated by spending policy for operations	<u>369</u>	<u>11,346</u>	<u>-</u>	<u>11,715</u>	<u>15,475</u>
Total investment return designated for operations	<u>\$ 5,617</u>	<u>\$ 11,346</u>	<u>\$ -</u>	<u>\$ 16,963</u>	<u>\$ 1,036</u>
Investment return in excess of amount designated for operations					
Dividends and interest (net of expenses of \$3,334 and \$3,863, respectively)	\$ 1,366	\$ 3,686	\$ -	\$ 5,052	\$ 8,771
Net investment appreciation (depreciation)	<u>5,557</u>	<u>156</u>	<u>-</u>	<u>5,713</u>	<u>(120,024)</u>
Total return on long-term investments	6,923	3,842	-	10,765	(111,253)
Investment return not designated by spending policy for operations	(5,216)	-	-	(5,216)	14,902
Investment return designated by spending policy for operations	<u>(369)</u>	<u>(11,346)</u>	<u>-</u>	<u>(11,715)</u>	<u>(15,475)</u>
Investment return in excess of amount designated for operations	<u>\$ 1,338</u>	<u>\$ (7,504)</u>	<u>\$ -</u>	<u>\$ (6,166)</u>	<u>\$ (111,826)</u>

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**6. Publications inventory, net**

As of September 30, 2009 and 2008, net publications inventory consisted of the following:

	2009	2008
Retail	\$ 1,158	\$ 1,382
Work-in-process	266	421
Consignment	248	302
Subtotal	1,672	2,105
Less: allowance for obsolescence	(390)	(433)
Total	<u>\$ 1,282</u>	<u>\$ 1,672</u>

**7. Other assets**

During fiscal 2009, the Gallery received real and personal property with an estimated fair value of \$3,300 at the date of donation. The Gallery has decided to dispose of the assets and is actively marketing them for sale.

**8. Fixed assets, net**

As of September 30, 2009 and 2008, net fixed assets consisted of the following:

	2009			2008
	Private Funds	Federal Funds	Total	Total
Buildings and improvements	\$ 156,310	\$ 144,164	\$ 300,474	\$ 272,384
Equipment	5,274	48,609	53,883	50,110
Construction-in-progress	-	7,181	7,181	25,828
Equipment under capital lease	-	2,962	2,962	2,962
Subtotal	161,584	202,916	364,500	351,284
Less: accumulated depreciation and amortization	(97,423)	(71,734)	(169,157)	(159,494)
Total	<u>\$ 64,161</u>	<u>\$ 131,182</u>	<u>\$ 195,343</u>	<u>\$ 191,790</u>

Depreciation and amortization expense was \$9,663 and \$9,819 for the years ended September 30, 2009 and 2008, respectively.



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**9. Contractual obligations**

The Gallery has entered into a number of contractual obligations with various parties for the acquisition of art for its collection. These contractual obligations are unsecured, non-interest bearing and require annual payments.

As of September 30, 2009 and 2008, contractual obligations consisted of the following:

	2009	2008
Contractual obligations	\$ 34,888	\$ 34,101
Less: discounts on contractual obligations	(1,200)	(2,293)
Total	<u>\$ 33,688</u>	<u>\$ 31,808</u>

Annual payments due during the next three years on contractual obligations are as follows:

	Annual Payments
2010	\$ 18,613
2011	8,325
2012	7,950
Total	<u>\$ 34,888</u>

**10. U.S. Government appropriations**

The Gallery's U.S. Government appropriation revenue recognized in fiscal year 2009 and 2008, are reconciled to the U.S. Government appropriations received as follows:

	2009			2008
	Operating	Renovation	Total	Total
U.S. Government appropriation revenue recognized	\$ 103,930	\$ 17,368	\$ 121,298	\$ 118,808
Unexpended obligations	6,721	-	6,721	5,985
Amounts expended from prior year's appropriations	(5,263)	-	(5,263)	(5,058)
Total U.S. Government appropriations	<u>\$ 105,388</u>	<u>\$ 17,368</u>	<u>\$ 122,756</u>	<u>\$ 119,735</u>

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The Gallery's federal expenses in fiscal year 2009 and 2008 are reconciled to the U.S. Government appropriations for fiscal year 2009 and 2008 as follows:

	2009			2008
	Operating	Renovation	Total	Total
Total federal expenses	\$ 107,024	\$ 5,561	\$ 112,585	\$ 109,780
Depreciation and amortization	(5,588)	(390)	(5,978)	(5,960)
Changes in unfunded liabilities	(439)	(780)	(1,219)	(2,327)
Unexpended obligations	6,721	7,760	14,481	5,985
Amounts expended from prior year's appropriations	(5,263)	-	(5,263)	(5,058)
Capital expenditures	2,933	5,217	8,150	17,315
Total U.S. Government appropriations	<u>\$ 105,388</u>	<u>\$ 17,368</u>	<u>\$ 122,756</u>	<u>\$ 119,735</u>

## 11. Net assets released from restrictions

Net assets are released from donor restrictions when the expenses are incurred to satisfy the restricted purposes as specified by donors. The donor-specified restrictions that were met in the reporting period are as follows:

	2009		2008	
	Operating	Non-operating	Operating	Non-operating
Acquisition of art	\$ -	\$ 20,502	\$ -	\$ 12,587
Collections	1,816	-	3,485	-
Special exhibitions	5,263	-	4,811	-
Education and public programs	4,098	-	5,234	-
Editorial and photography	549	-	262	-
Capital projects	-	100	-	434
Operations	6,579	-	3,961	-
Subtotal private funds	<u>18,305</u>	<u>20,602</u>	<u>17,753</u>	<u>13,021</u>
Special exhibitions	3,388	-	3,419	-
Capital projects	-	13,993	-	19,566
Subtotal federal funds	<u>3,388</u>	<u>13,993</u>	<u>3,419</u>	<u>19,566</u>
Total	<u>\$ 21,693</u>	<u>\$ 34,595</u>	<u>\$ 21,172</u>	<u>\$ 32,587</u>

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**12. Analysis of restricted net assets**

As of September 30, 2009 and 2008, temporarily restricted net assets and the investment income from permanently restricted net assets are restricted to support the following purposes:

	2009		2008	
	Temporarily Restricted	Permanently Restricted	Temporarily Restricted	Permanently Restricted
Acquisition of art	\$ 34,026	\$ 69,841	\$ 38,452	\$ 69,755
Collections	4,526	34,130	5,076	34,715
Special exhibitions	7,249	31,142	10,160	30,363
Education and public programs	33,139	83,644	30,634	89,377
Editorial and photography	317	3,498	628	-
Capital projects	577	-	937	-
Operations	36,528	143,093	35,489	148,518
Subtotal private funds	116,362	365,348	121,376	372,728
Special exhibitions	12	-	50	-
Capital projects	15,035	-	11,660	-
Subtotal federal funds	15,047	-	11,710	-
Total	\$ 131,409	\$ 365,348	\$ 133,086	\$ 372,728

**13. Employee benefits**

Total pension expense recognized in the Gallery's financial statements was \$6,727 and \$6,318 for the years ended September 30, 2009 and 2008, respectively. These amounts do not include pension expense financed by OPM and imputed to the Gallery of \$1,810 and \$1,570 respectively. To the extent that Gallery employees are covered by the thrift savings component of FERS, the Gallery's payments to the plan are recorded as operating expenses. The Gallery's costs associated with the thrift savings component of FERS for the years ended September 30, 2009 and 2008, were \$2,085 and \$1,912, respectively.

In addition, the Gallery makes matching contributions for all employees who are eligible for current health and life insurance benefits. The Gallery's contributions for active employees are recognized as operating expenses. During fiscal years 2009 and 2008, the Gallery contributed \$4,821 and \$4,517, respectively. Using the cost factors supplied by OPM, the Gallery has not recognized as an expense in its financial statements the future cost of post-retirement health benefits and life insurance for its employees. These costs amounted to approximately \$5,952 and \$5,399 during fiscal years 2009 and 2008 respectively, and are financed by OPM and imputed to the Gallery.

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The Gallery has a commitment to certain key employees whereby the Gallery will pay those employees a specified amount at a future point in time. The cost of these benefits is accrued over the key employees' future years of service to the Gallery. The cost of these benefits for fiscal years 2009 and 2008 total \$420 and \$507, respectively, and is recognized as an expense in the statement of activities and as a liability included in accounts payable and accrued expenses in the accompanying statement of financial position.

**14. Income taxes**

The Gallery is a nonprofit organization exempt from federal income taxes under the provisions of Section 501(c)(3) of the Internal Revenue Code.

On October 1, 2008, the Gallery adopted the provisions of ASC Topic 740-10-25, *"Income Taxes Recognition"* (ASC Topic 740-10-25"). ASC Topic 740-10-25 requires that a tax position be recognized or derecognized based on a more-likely-than-not threshold. This applies to positions taken or expected to be taken in a tax return. The implementation of ASC Topic 740-10-25 had no impact on the Gallery's financial statements. The Gallery does not believe its financial statements include any uncertain tax positions.

**15. Lease commitments**

During fiscal year 2002, the Gallery entered into a capital lease obligation in connection with the installation of equipment. The Gallery has also entered into several operating leases for warehouse and office space, which continue through January 31, 2018. The terms of these operating leases include additional rent for operating expenses, real estate taxes, utilities and maintenance. Future minimum lease payments under these leases for the fiscal years ended September 30 are as follows:

	2009	
	Capital Lease	Operating Leases
2010	\$ 342	\$ 3,592
2011	342	3,677
2012	342	3,763
2013	344	1,767
2014	344	889
Thereafter	345	4,023
Total minimum lease payments	2,059	\$ <u>17,711</u>
Less: amount representing interest	<u>(343)</u>	
Present value of minimum capital lease payments	<u>\$ 1,716</u>	

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Rental expense was approximately \$4,830 and \$4,528 for the years ended September 30, 2009 and 2008, respectively.

**16. Fair Value Measurements**

The Gallery adopted the provisions of ASC Topic 820, “*Fair Value Measurements and Disclosures*” (ASC Topic 820), effective October 1, 2008. ASC Topic 820 requires disclosures of financial position in periods subsequent to initial recognition, whether the measurements are made on a recurring basis or a nonrecurring basis, establishes a framework based on the observability of inputs used for measuring fair value and expands disclosure about fair market value measurements. Under ASC Topic 820, fair value is defined as the price that would be received to sell an asset or paid to transfer a liability (i.e., the “exit price”) in an orderly transaction between market participants at the measurement dates.

The fair value hierarchy is categorized into three levels based on the inputs as follows:

Level 1 - Valuations based on unadjusted quoted prices in active markets for identical assets or liabilities that the Gallery has the ability to access as of the reporting date. Valuation adjustments and block discounts are not applied to Level 1 securities. Since valuations are based on quoted prices that are readily and regularly available in an active market, valuation of these securities does not entail a significant degree of judgment.

Level 2 - Valuations based on quoted prices in markets that are not active or for which all significant inputs are observable, either directly or indirectly as of the reporting date.

Level 3 - Valuations based on inputs that are unobservable and significant to the overall fair value measurement as of the reporting date. The determination of fair value for these financial instruments requires one or more inputs subject to significant management judgment or estimation.

The following table identifies those assets reported at fair value and are subject to the hierarchy outlined above as of September 30, 2009:

	Pledges Receivable, net	Investments	Trusts Held by Others	Deferred Charges and Other Assets
Items reported at fair value	\$ 17,118	\$ 579,010	\$ 11,207	\$ 3,888
Items not subject to fair value reporting	-	5,000	-	677
Total	<u>\$ 17,118</u>	<u>\$ 584,010</u>	<u>\$ 11,207</u>	<u>\$ 4,565</u>

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Items not subject to fair value reporting consist of the loan to the U.S. Treasury and deferred charges.

The following table summarizes the fair value measurement as of September 30, 2009 for financial assets by pricing observability levels:

	Prices in Active Markets for Identical Assets (Level 1)	Other Observable Inputs (Level 2)	Unobservable Inputs (Level 3)	Fair Value at 9/30/09
Common and preferred stocks	\$ 69,255	\$ -	\$ -	\$ 69,255
Mutual funds	136,784	-	-	136,784
Public and equity funds	-	-	192,997	192,997
Hedge funds	-	-	108,934	108,934
Multi-asset class	-	-	40,468	40,468
Private equity and venture capital	-	-	30,572	30,572
Trust held by others	-	-	8,661	8,661
Assets measured at fair value on a recurring basis	206,039	-	381,632	587,671
Pledge receivables	-	-	17,118	17,118
Trust held by others	-	-	2,546	2,546
Deferred charges and other assets	-	-	3,888	3,888
Assets measured at fair value on a non-recurring basis	-	-	23,552	23,552
Total assets measured at fair value	\$ 206,039	\$ -	\$ 405,184	\$ 611,223

In general for Level 3 investments, the Gallery utilizes the investment manager of the asset to provide a valuation estimate based on previously disclosed techniques and processes which have been reviewed for propriety and consistency with consideration given to asset type and investment strategy. Management makes best estimates based on information available. The following estimates and assumptions were used to determine the fair value of each class of financial instruments listed above:

Equity Investments - Equity investments include but are not limited to separately held accounts in hedge funds and limited partnership holdings. These assets which are grouped by investment objective consist of both publicly traded and privately-held securities, diversified globally.

- Publicly traded securities – These investments generally include fixed income securities, convertible bonds and global equity holdings. Securities traded on an active exchange are priced using unadjusted market quotes for identical assets and are classified as Level 1.

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- Privately-held securities – These investments generally include hedge funds, multi-asset class, private equity and venture capital funds. These funds are privately held and trade infrequently, if at all. The valuations are calculated by the investment manager based on valuation techniques that take into account each fund's underlying assets and include traditional valuation methods such as the market, cost and income approaches. The valuation policies adopted by the manager are reviewed by the Gallery for propriety, consistency, compliance and completeness. Limited partnerships and other non-redeemable funds are classified as Level 3. No active market exists for these assets and their valuations are based on unobservable and/or significantly adjusted inputs. Additionally in the case of private equity and venture capital investments there are limited options to transfer or withdraw from these funds prior to their termination. Inputs used to determine fair value are based upon the best available information provided by the partnerships/funds and may incorporate management assumptions and best estimates after considering a variety of internal and external factors.

Trusts Held by Others – Assets managed under trust agreements from donors where the Gallery is the beneficiary of the income are categorized as Level 3. For those trust agreements where the Gallery is the beneficiary, those assets are valued based on property valuations that involve significant judgment and estimation, and therefore are included in Level 3.

Deferred Charges and Other Assets – For those arrangements where the Gallery has received real and personal property, the assets are valued based on property valuations that involve significant judgment and estimation, and therefore is included in Level 3.

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The following table summarizes the changes in Level 3 assets, measured at fair value on a recurring basis, as of September 30, 2009:

	Public and Equity Funds	Hedge Funds	Multi -Asset Class	Private Equity and Venture Capital Funds	Trust Held by Others
Fair value of Level 3 assets at September 30, 2008	\$ 181,338	\$ 121,827	\$ 43,487	\$ 33,119	\$ 8,444
Net unrealized / realized gains (losses)	5,889	3,967	(3,019)	(8,235)	217
Proceeds from sales, redemptions and distributions	(14,230)	(16,860)	-	(555)	-
Purchase of investments	20,000	-	-	6,243	-
Fair value of Level 3 assets at September 30, 2009	<u>\$ 192,997</u>	<u>\$ 108,934</u>	<u>\$ 40,468</u>	<u>\$ 30,572</u>	<u>\$ 8,661</u>

Total gains and losses for Level 3 assets included in changes in net assets for the year ended September 30, 2009 as follows:

	Pledges Receivable, net	Investments	Trusts Held by Others	Deferred Charges and Other Assets
Total gains (losses)	<u>\$ 9,436</u>	<u>\$ (674)</u>	<u>\$ 667</u>	<u>\$ -</u>

The change in unrealized gains relating to assets valued on a recurring basis held at September 30, 2009 was \$9,946.

**Fair Value Options**

In February 2007, the FASB updated GAAP with ASC Topic 825-10-25 “*Financial Instruments - Recognition*”. The fair value option permits entities to choose to measure eligible items at fair value at specific election dates, with subsequent unrealized gains and losses reported in the entity’s statement of activities. The Gallery adopted this standard effective October 1, 2008. The Gallery assessed the fair value options made available under the standard and elected not to apply the fair value option to any financial instruments that were not already recognized at fair value.



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**17. Endowments**

The Gallery's endowment consists of 64 individual funds established for a variety of purposes. Its endowment includes both donor-restricted endowment funds and funds designated by the Board of Trustees to function as endowments. As required by GAAP, net assets associated with endowment funds, including funds designated by the Board of Trustees to function as endowments, are classified and reported based on the existence or absence of donor-imposed restrictions.

On January 23, 2008, the District of Columbia adopted UPMIFA, the provisions of which apply to funds existing on or established after that date and to decisions made and actions taken after that date. The Gallery has interpreted UPMIFA as requiring the preservation of the fair value of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Gallery classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure by the Gallery in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, the Gallery considers the following factors when making a determination to appropriate or accumulate donor-restricted funds:

- The duration and preservation of the fund
- The purposes of the Gallery and the donor-restricted endowment fund
- General economic conditions
- The possible effect of inflation and deflation
- The expected total return from income and the appreciation of investments
- Other resources of the Gallery
- The investment policies of the Gallery

Upon the adoption of UPMIFA and ASC Topic 958-205-45, the Gallery was required to reflect a retrospective reclassification of net assets from unrestricted to temporarily restricted of approximately \$4,862.

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Endowment net assets were comprised of the following as of September 30, 2009 and 2008:

	2009		2008	
	Donor-restricted endowment funds	Board-designated endowment funds	Donor-restricted endowment funds	Board-designated endowment funds
Unrestricted	\$ (42,882)	\$ 12,706	\$ (46,251)	\$ 12,298
Temporarily restricted	29,756	-	30,111	-
Permanently restricted	365,348	-	372,728	-
Total funds	<u>\$ 352,222</u>	<u>\$ 12,706</u>	<u>\$ 356,588</u>	<u>\$ 12,298</u>

The following table summarizes the change in the endowment funds during the year ended September 30, 2009:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets as of October 1, 2008	<u>\$ (33,953)</u>	<u>\$ 30,111</u>	<u>\$ 372,728</u>	<u>\$ 368,886</u>
Investment return:				
Investment Income	106	3,204	-	3,310
Net appreciation (depreciation)	3,458	(312)	86	3,232
Total investment return	<u>3,564</u>	<u>2,892</u>	<u>86</u>	<u>6,542</u>
Contributions	-	-	792	792
Re-instatement of endowment through liquidation of an asset	-	1,944	-	1,944
Appropriation of endowment assets for expenditures	(219)	(4,726)	(8,498)	(13,443)
Reclassifications	<u>432</u>	<u>(465)</u>	<u>240</u>	<u>207</u>
Endowment net asset as of September 30, 2009	<u>\$ (30,176)</u>	<u>\$ 29,756</u>	<u>\$ 365,348</u>	<u>\$ 364,928</u>

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The following table summarizes the change in the endowment funds during the year ended September 30, 2008:

	Unrestricted	Temporarily Restricted	Permanently Restricted	Total
Endowment net assets as of October 1, 2007	\$ 23,241	\$ 56,737	\$ 368,846	\$ 448,824
Net classifications based on the change in accounting principles	<u>(4,862)</u>	<u>4,862</u>	<u>-</u>	<u>-</u>
Endowment net assets after reclassification	<u>18,379</u>	<u>61,599</u>	<u>368,886</u>	<u>448,824</u>
Investment return:				
Investment Income	566	3,906	-	4,472
Net appreciation (depreciation)	<u>(53,308)</u>	<u>(22,423)</u>	<u>(1,715)</u>	<u>(77,446)</u>
Total investment return	<u>(52,742)</u>	<u>(18,517)</u>	<u>(1,715)</u>	<u>(72,974)</u>
Contributions	-	-	8,255	8,255
Bad debt expense	-	-	(2,000)	(2,000)
Release of restrictions for capital expenditures	132	(132)	-	-
Appropriation of endowment assets for expenditures	(157)	(13,198)	-	(13,355)
Reclassifications	<u>435</u>	<u>359</u>	<u>(658)</u>	<u>136</u>
Endowment net asset as of September 30, 2008	<u>\$ (33,953)</u>	<u>\$ 30,111</u>	<u>\$ 372,728</u>	<u>\$ 368,886</u>

**Funds with Deficiencies**

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the level that the donor requires the Gallery to retain as a fund of perpetual duration. Deficiencies of this nature that are reported in unrestricted net assets were \$42,882 as of September 30, 2009. These deficiencies were the result of unfavorable market fluctuations that occurred shortly after the investment of new contributions and continued appropriation for certain programs that was deemed prudent by the Gallery. Subsequent gains that restore the fair value of the assets of the endowment fund to the required level will be classified as an increase in unrestricted net assets.

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**Return Objectives and Risk Parameters**

The Gallery has adopted investment and spending policies for endowment assets that provides for the continued financial stability of the Gallery and a revenue stream for funding the Gallery's mission. Endowment assets include those assets of donor restricted funds that the organization must hold in perpetuity as well as board-designated funds. Under this policy, as approved by the Board of Trustees, the endowment assets are invested in a manner that ensures safety through diversification while obtaining a competitive rate of return. The Gallery expects its endowment funds over time, to provide an average rate of return of approximately 5.0% annually. Actual returns in any year may vary from this amount.

**Strategies Employed for Achieving Objectives**

To satisfy its long-term rate-of-return, the Gallery relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized) and current yields (interest and dividends). The Gallery targets diversified asset allocation that utilizes fixed income and equity-based investments to achieve its long-term objectives within prudent risk constraints.

**Spending Policy and How the Investment Objectives Relate to Spending Policy**

The Gallery's spending policy is based on an annual endowment spending rate of 5% of the average fair value of endowment investments at the end of the previous three-and-one quarter years. This spending rate constitutes the Board's annual appropriation for spending endowment earnings to support the purchase of art and for the support of operations. This spending assumption is intended to allow for the spending of the income of the portfolio, provide a target rate of return for the fund, and provide a sustainable spending level that will allow for support of the Gallery's initiatives in the accomplishment of its mission, while maintaining the purchasing power of the endowment fund's assets.

**18. Subsequent Events**

The Gallery has performed an evaluation of subsequent events through November 16, 2009, which is the date the financial statements were available to be issued, noting no events which affect the financial statements as of September 30, 2009.